

39. We find that access to this non-substitutable programming is necessary for competition in the video distribution market to remain viable. An MVPD's ability to compete will be significantly harmed if denied access to popular vertically integrated programming for which no good substitute exists.<sup>193</sup> Because the exclusive contract prohibition applicable to satellite-delivered programming has been in effect since 1992, we do not have specific empirical evidence of the impact of withholding of satellite-delivered programming. However, for vertically integrated programming that is delivered terrestrially and therefore beyond the scope of Section 628(c)(2)(D), there is factual evidence that cable operators have withheld this programming from competitors and, in two instances – in San Diego and Philadelphia – there is empirical evidence that such withholding has had a material adverse impact on competition in the video distribution market. In the *Adelphia Order*, the Commission conducted an analysis which concluded that lack of access to RSN programming can decrease an MVPD's market share significantly because a large number of consumers will refuse to purchase the MVPD's service and will instead elect to purchase service from the cable operator that offers the RSN.<sup>194</sup> The analysis concluded that, without access to the cable-affiliated RSN in Philadelphia, the percentage of television households

(Continued from previous page)

marketplace.”): *infra* ¶ 39 (discussing impact on competitive MVPD subscribership from withholding of cable-affiliated programming).

<sup>193</sup> See 2002 Extension Order, 17 FCC Rcd at 12138, ¶ 32; *Adelphia Order*, 21 FCC Rcd at 8287, ¶ 189; *id.* at 8258-59, ¶ 124 (stating that “RSNs are often considered ‘must-have’ programming. . . . Hence, an MVPD’s ability to gain access to RSNs and the price and other terms of conditions of access can be important factors in its ability to compete with rivals”); *Hughes Order*, 19 FCC Rcd at 535, ¶ 133 (stating that “the basis for the lack of adequate substitutes for regional sports programming lies in the unique nature of its core component: RSNs typically purchase exclusive rights to show sporting events, and sports fans believe that there is no good substitute for watching their local and/or favorite team play an important game”); 12<sup>th</sup> Annual Report, 21 FCC Rcd at 2596, ¶ 205 (“Access to must have programming, including major national cable networks and regional sports networks, on a timely basis and at competitive rates is a key competitive issue for all MVPDs.”); see also AT&T Comments at 11 (“MVPDs still remain highly dependent on key programming owned by the established cable MSOs, including TBS, Discovery, TNT, CNN, TLC, and other popular basic cable networks, and also the regional sports network programming that the Commission found, in the *Adelphia Order*, could be used as a powerful weapon against potential competitors.”); EchoStar Comments at 7 (“Withholding a single ‘must have’ programming network from competitive MVPD platforms can hamper, if not foreclose, the development and preservation of viable competition.”). Numerous competitive MVPDs cite certain national programming networks as “must have” programming. See NRTC Comments at 20 (stating that an MVPD cannot “operate successfully” if that system lacks access to cable-affiliated networks such as CNN, HBO, TNT, and The Discovery Channel); SureWest Comments at 3 (“no MVPD could survive without access to the most popular, ‘must-have,’ programming channels such as CNN, TNT and HBO”); Qwest Comments at 5 (“Since subscribers ultimately are most interested in content, Qwest’s ability to serve its customers is tied directly to its access to ‘must-have’ vertically integrated programming, including CNN, HBO, TNT, IN DEMAND pay-per-view content, Discovery, and regional sports networks.”). Numerous competitive MVPDs also cite sports programming as “must have” programming. See AT&T Comments at 15 (stating that Congress and the Commission “have continued to recognize on multiple occasions the ‘must have’ nature of cable incumbents’ regional sports networks”); BSPA Comments at 6; RCN Comments at 4 (“‘Must have’ programming is programming that has no close substitutes and cannot be duplicated no matter how much time and money are committed. Clearly, sports programming is ‘must have’ programming.”); SureWest Comments at 3 (“sports programming is also core to an MVPD’s survival in a competitive market”); USTelecom Comments at 14-15; Verizon Comments at 9 (stating that regional sports programming “is a key component of a competitive multichannel video service”).

<sup>194</sup> *Adelphia Order*, 21 FCC Rcd at 8267-72, ¶¶ 140-51 and 8341-50, Appendix D; see *id.* at 8271-72, ¶ 151 (“We conclude that there is substantial evidence that a large number of consumers will refuse to purchase DBS service if the provider cannot offer an RSN.”); *Hughes Order*, 19 FCC Rcd at 546-47, ¶ 159 (stating that withholding of RSN programming will cause consumers to lose access to highly desired programming and some consumers will leave their preferred MVPD provider to access the foreclosed programming on a less-desired MVPD platform).

that subscribe to DBS service in Philadelphia is 40 percent below what would otherwise be expected.<sup>195</sup> In San Diego, the analysis concluded that lack of access to the cable-affiliated RSN results in a 33 percent reduction in the households subscribing to DBS service.<sup>196</sup> We also believe that a competitive MVPD's lack of access to popular non-RSN networks would not have a materially different impact on the MVPD's subscribership than would lack of access to an RSN. We are unaware of examples of nationally distributed programming being withheld from willing buyers as has occurred with some RSNs. Instead, we must turn to indirect evidence of the popularity of nationally distributed programming networks. A number of networks receive ratings higher than or equal to those of RSNs that are currently withheld from DBS providers.<sup>197</sup> While ratings are not a perfect predictor of consumer response to the withholding of a network, they do provide us with sufficient evidence to conclude that some nationally distributed networks are sufficiently valuable to viewers such that some viewers may switch to an alternative MVPD if the popular programming were not made available on their current MVPD.

40. We disagree with Cablevision's criticisms of the Commission's analysis in the *Adelphia Order*.<sup>198</sup> In that decision, the Commission conducted a statistical (regression) analysis which found, after holding other relevant factors constant, that non-cable MVPDs had significantly lower market shares in markets where they were denied access to an RSN.<sup>199</sup> As a threshold matter, the Commission's regression analysis is just one component of an economic analysis of a possible "uniform price increase strategy" that a cable operator (in particular, one of the applicants to acquire Adelphia cable systems) might follow with regard to RSNs. Under this scenario, a vertically integrated cable operator that has just increased the number of homes that it passes in a market where it also owns an RSN raises the price of the RSN to all MVPDs in the market, but not by an amount large enough to induce the rival MVPD in the market to stop carrying the RSN. The question posed by the analysis is whether this (sustainable) price increase is greater than the five percent level specified in the Department of Justice ("DOJ") Merger Guidelines. In the *Adelphia Order*, the Commission stated that "price increases of five percent or more would likely harm rival MVPDs' ability to compete and/or be passed on to consumers in some form, such

<sup>195</sup> See *Adelphia Order*, 21 FCC Rcd at 8271, ¶ 149.

<sup>196</sup> See *id.* We also note that, according to data from Nielsen Media Research, in two cities where most competitive MVPDs are unable to access the cable-affiliated RSN (Philadelphia and San Diego), the collective market share of competitive MVPDs is well below their national average of 33 percent: Philadelphia (19.8 percent) and San Diego (13.7 percent). See DMA Household Universe Estimates July 2007: Cable And/Or ADS (Alternate Delivery Systems), [http://www.tvb.org/nav/build\\_frameset.asp](http://www.tvb.org/nav/build_frameset.asp) (follow "Research Central" hyperlink; then follow "Market Track" hyperlink; then follow "Cable and ADS Penetration by DMA" hyperlink) (last visited Aug. 2, 2007); see also AT&T Comments at 17 (noting that DIRECTV's market share in San Diego is half of its national average); CA2C Comments at 9, 16; USTelecom Comments at 15; AT&T Reply Comments at 5 (stating that DBS subscription is lower in Philadelphia where Comcast has refused to provide RSN access). While Cablevision notes that DBS market penetration has in fact tripled in Philadelphia from 4 percent in 2000 to 12 percent at the end of 2006 despite the inability of DBS operators to access an RSN (see Cablevision Comments at 25; Cablevision Reply Comments at 12), cable market penetration is still significantly greater in Philadelphia (81.1 percent) than in metropolitan areas with a population similar to that of Philadelphia: Phoenix (70.1 percent), San Antonio (70.8 percent); and Dallas (53.5 percent). See *id.*

<sup>197</sup> According to data collected by Nielsen, Comcast SportsNet earned a 1 rating and 2 share in the all-day time period during the May 2006 ratings period in the Philadelphia DMA. Three programming networks earned superior ratings or shares while six networks earned equivalent ratings and shares. In the San Diego DMA during the same period, four programming networks earned ratings and shares equivalent to those earned by San Diego Channel 4, the RSN which carries San Diego Padres baseball games.

<sup>198</sup> See Cablevision Comments, Appendix B at 24-25.

<sup>199</sup> *Adelphia Order*, 21 FCC Rcd at 8267-72, ¶¶ 140-51 and 8341-50, Appendix D.

as increased rates or reductions in quality or customer service.”<sup>200</sup> In other words, based on the analysis in the *Adelphia Order* showing that RSN prices would rise significantly in several markets post-merger, the Commission concluded that MVPD customers would be harmed. One of several parameters needed to assess the uniform price increase scenario is the amount by which subscribership to a competitive MVPD would fall if that MVPD were to choose not to carry the RSN. Cablevision’s critique does not address the full uniform price increase analysis. Rather, it focuses on the regression equation. Cablevision offers several criticisms of the regression model, most of which amount to the assertion that some relevant explanatory variables were left out of the equation. These and other criticisms are addressed in detail in Appendix B. As explained therein, some of the variables claimed to be left out were, in fact, included. Moreover, even if some relevant variables were left out, that does not, in and of itself, indicate that the coefficients on the relevant dummy variables are inaccurate or biased. Moreover, we have estimated additional regression equations designed to include some of the variables that Cablevision claims should have been included. The new results, in fact, support the Commission’s analysis in the *Adelphia Order*, and in some respects strengthen the conclusions reached in that decision. In sum, we do not find persuasive the Cablevision critique of our analysis in the *Adelphia Order*, including the regression analysis. We remain convinced that the regression analysis demonstrates that, with regard to RSNs and programming with similar characteristics (such as popularity and similar monthly per subscriber affiliate fee and network advertising revenue), withholding programming from rivals can be a profitable strategy for a vertically integrated cable programmer and that such withholding can have a significant impact on subscribership to the rival MVPDs. Such practices, in turn, predictably harm competition and diversity in the distribution of video programming, to the detriment of consumers.

41. We find that access to vertically integrated programming is essential for new entrants in the video marketplace to compete effectively. If the programming offered by a competitive MVPD lacks “must have” programming that is offered by the incumbent cable operator, subscribers will be less likely to switch to the competitive MVPD.<sup>201</sup> We give little weight to the claims by cable operators that recent entrants, such as telephone companies, have not experienced “any trouble” to date in acquiring access to satellite-delivered vertically integrated programming.<sup>202</sup> As an initial matter, we note that competitive MVPDs state that they pay significant amounts for access to satellite-delivered vertically integrated programming.<sup>203</sup> Moreover, because the exclusive contract prohibition is currently in effect and has been since 1992, vertically integrated programmers delivering programming to MVPDs via satellite were not able to deny competitors access to their programming.<sup>204</sup> As discussed in Section III.A.3.b below, however, there is substantial evidence that, when the exclusive contract prohibition does not apply, such as in the case of terrestrially delivered programming, vertically integrated programmers may have an

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<sup>200</sup> See *id.* at 8269, ¶ 143.

<sup>201</sup> See *2002 Extension Order*, 17 FCC Rcd at 12139, ¶ 34; *Adelphia Order*, 21 FCC Rcd at 8267-72, ¶¶ 140-51 and 8341-50, Appendix D: *supra* ¶ 39 (discussing impact on competitive MVPD subscribership from withholding of cable-affiliated programming).

<sup>202</sup> See Comcast Comments at 21; Comcast Reply Comments at 17; *but see* AT&T Reply Comments at 10 (“AT&T and Verizon already have experienced the cold shoulder in trying to obtain regional sports programming from incumbent cable operators.”).

<sup>203</sup> See EchoStar Reply Comments at 19 (stating that cable operators repeatedly increase license fees for their affiliated networks); *see also* AT&T Comments at 11 (stating that RCN has told investors that it pays 37 percent of its revenues to Time Warner and Comcast for programming).

<sup>204</sup> See Verizon Comments at 3 (noting that it has not faced difficulty in obtaining satellite-delivered vertically integrated programming while the exclusive contract prohibition is in effect, but that it expects the situation to change if the prohibition were allowed to sunset).

incentive to withhold programming from these recent entrants.<sup>205</sup> We also reject the cable MSOs' suggestion that the resources of some competitors in the video distribution market (*i.e.*, telephone companies) should change our analysis of whether to extend the prohibition at this time.<sup>206</sup> The competitors to which the cable operators refer are new entrants to the video distribution market, and have no established customer base. If cable operators have exclusive access to content that is essential for viable competition and for which there are no close substitutes, and they have the incentive to withhold such content, they can significantly impede the ability of new entrants to compete effectively in the marketplace, regardless of their level of resources.<sup>207</sup> As we concluded in the *Adelphia Order*, excluding "must have" cable-affiliated content from DBS operators has reduced the percentage of households that subscribe to DBS service to as much as 40 percent below what would otherwise be expected.<sup>208</sup>

42. For the reasons discussed above, we conclude that there are no close substitutes for some satellite-delivered vertically integrated programming and that such programming is necessary for viable competition in the video distribution market.<sup>209</sup> Having made this determination, we further conclude that vertically integrated programmers continue to have the ability to favor their affiliated cable operators over competitive MVPDs such that competition and diversity in the distribution of video programming would not be preserved and protected.<sup>210</sup> Accordingly, assuming vertically integrated programmers continue to have the incentive to favor their affiliated cable operators, allowing vertically integrated programmers to enter into exclusive arrangements with their affiliated cable operators will fail to protect and preserve competition and diversity in the distribution of video programming.<sup>211</sup>

#### **b. Incentive**

43. We next assess whether vertically integrated programmers continue to have the incentive to favor their affiliated cable operators over competitive MVPDs.<sup>212</sup> This requires us to analyze (i) whether cable operators, through the number of subscribers they serve, the number of homes they pass, and their affiliations with programmers, continue to have market dominance of sufficient magnitude that, in the absence of the prohibition, they would be able to act in an anticompetitive manner; and (ii) whether there continues to be an economic rationale for vertically integrated programmers to engage in exclusive agreements with cable operators that will cause such anticompetitive harms.<sup>213</sup> As discussed in this

<sup>205</sup> See *infra* Section III.A.3.b.

<sup>206</sup> See Cablevision Comments at 2, 5; Comcast Comments at 20; Time Warner Reply Comments at 21.

<sup>207</sup> See Verizon Reply Comments at 11-12.

<sup>208</sup> See *Adelphia Order*, 21 FCC Rcd at 8271, ¶ 149. As competitive MVPDs note, DBS providers have been able to attract and retain millions of subscribers because of their ability to offer "must have" programming that is affiliated with cable operators. See AT&T Comments at 10 n.25; CA2C Comments at 12. Moreover, we note that the Commission has attributed the increased growth of DBS subscribership in part to the ability of DBS operators to offer local broadcast signals, which Cablevision has referred to as "must have" content. See *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Eleventh Annual Report, 20 FCC Rcd 2755, 2792 ¶ 54 (2005); Comments of Cablevision Systems Corp., MB Docket No. 03-124 (June 16, 2003) at 3, 13-14, 18, 28 (referring to the Fox broadcast network as "must have").

<sup>209</sup> See 2002 *Extension Order*, 17 FCC Rcd at 12135, ¶ 24.

<sup>210</sup> See *id.*

<sup>211</sup> See *id.*

<sup>212</sup> See *id.* at 12139-40, ¶ 35.

<sup>213</sup> See *id.*

section, we conclude that vertically integrated programmers continue to have the incentive to favor their affiliated cable operators over competitive MVPDs.

44. We briefly reiterate here how a vertically integrated cable programmer might attempt to harm the ability of rival MVPDs to compete through the use of exclusive contracts.<sup>214</sup> An exclusive arrangement between a cable-affiliated programmer and its affiliated cable operator will reduce the number of platforms distributing the cable-affiliated programming network and thus the total number of subscribers to the network. This results in a reduction in potential advertising or subscription revenues that would otherwise be available to the network. In the long term, however, the cable-affiliated programmer would gain from an increased number of subscribers as customers switch to the affiliated cable distribution service in order to receive the exclusive programming. Thus, an exclusive contract is a kind of “investment,” in which an initial loss of profits from programming is incurred in order to achieve higher profits later from increased cable distribution. This type of arrangement is most profitable when the costs of the investment are low and its benefits are high. The costs are lowest when the initial loss in programming revenue is low, such as when the rival distributors that are excluded serve relatively fewer customers. The benefits of the investment tend to be highest when the vertically integrated cable programmer ultimately expects to serve a large number of subscribers, and will be able to charge them substantially more for cable distribution service than it could if it faced a strong rival distribution platform. We explained that the number of subscribers that a vertically integrated cable programmer serves is of particular importance in calculating the benefits of withholding programming from rival MVPDs. The larger the number of subscribers controlled by the vertically integrated cable programmer, the larger the benefits of withholding that accrue to that programmer. Thus, as the number of subscribers rises, so does the likelihood that withholding would be profitable.

45. In their comments, cable MSOs assert that they do not have an economic incentive to enter into exclusive programming agreements. First, they argue that they do not have a sufficient share of the MVPD market to make withholding of vertically integrated programming a profitable strategy.<sup>215</sup> Cablevision notes that the success of an exclusivity strategy depends on the ability of a vertically integrated programmer to recover a substantial portion of its lost revenues through increased distribution revenues.<sup>216</sup> As the number of subscribers to competing distributors rises, the likelihood of a successful withholding strategy decreases.<sup>217</sup> Cablevision contends that the nearly fifty percent increase in the number of customers served by rival MVPDs since 2002 has substantially increased the costs of an exclusivity strategy.<sup>218</sup> Second, cable MSOs argue that a typical programming network, no matter the ownership structure, will not foreclose opportunities to be as widely distributed as possible on multiple platforms.<sup>219</sup> Cablevision notes that a cable-affiliated programmer that enters into an exclusive arrangement with its affiliated distributor would risk being unable to recoup the significant license fees and advertising revenues that it loses by refusing access to competing platforms.<sup>220</sup> Cable MSOs claim that the over 30 million subscribers served by competitive MVPDs today represent a significant revenue

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<sup>214</sup> See *id.* at 12140-41, ¶¶ 36-39.

<sup>215</sup> See Cablevision Comments at 16 and Appendix B at 11.

<sup>216</sup> See *id.*

<sup>217</sup> See *id.*

<sup>218</sup> See *id.* at 17.

<sup>219</sup> See Cablevision Comments at 4; Comcast Comments at 21-22; Comcast Reply Comments at 22; NCTA Reply Comments at 6.

<sup>220</sup> See Cablevision Comments at 16.

source that no programmer can afford to ignore.<sup>221</sup> Third, cable MSOs argue that competitive MVPDs in response to an exclusive arrangement are likely to engage in competitive counter-measures, such as cutting prices, acquiring other programming on an exclusive basis, or launching new services of their own.<sup>222</sup>

46. Competitive MVPDs argue that vertically integrated cable programmers continue to have powerful incentives to withhold vertically integrated programming to impede the viability of competitors.<sup>223</sup> CA2C cites an April 2005 GAO Report which concludes that DBS operators have relatively fewer subscribers in urban and suburban markets where they face a content disadvantage compared to the incumbent cable operator.<sup>224</sup> CA2C also notes that DBS market share in Philadelphia and San Diego drops almost in half due to the lack of access to RSNs as compared to other similar high-density markets where DBS operators have access to RSNs.<sup>225</sup>

47. Competitive MVPDs disagree with claims by cable MSOs that the decrease in the collective market share of cable operators between 2002 and 2005 means they can no longer profitably withhold affiliated programming. First, they note that the 67 percent share of MVPD subscribers held by the cable industry remains the dominant market position.<sup>226</sup> Second, they argue that the increase in horizontal consolidation of the cable industry increases the ability for cable MSOs to leverage power collectively through “cable only” exclusives – *i.e.*, the withholding of programming from rival MVPDs while selling it to other cable operators with which they do not compete.<sup>227</sup> For example, competitive MVPDs note that Comcast makes Comcast SportsNet Philadelphia available to all Philadelphia-area cable operators, but not to DIRECTV or EchoStar.<sup>228</sup> They also emphasize that while the market share of small-to-medium sized, non-vertically integrated cable operators has declined, the market share of the four largest vertically integrated cable operators has increased substantially since 2002.<sup>229</sup> Third, they point to an increase in regional clustering, which, they say, has increased the market share of individual cable operations within the footprints of regional programming and created expanded opportunities to implement exclusive arrangements.<sup>230</sup> In response to these concerns, Comcast notes that both the Commission and the Director of the Bureau of Economics of the Federal Trade Commission (“FTC”)

<sup>221</sup> See *id.* at 20; NCTA Comments at 6.

<sup>222</sup> See Cablevision Comments at 8, 17; Cablevision Reply Comments at 11-12.

<sup>223</sup> See AT&T Comments at 3, 18; BSPA Comments at 3, 10; CA2C Comments at 7-8; Qwest Comments at 3 & n.6; USTelecom Comments at 4-5, 7; Verizon Comments at 5; see also Consumer Groups Reply Comments at 5.

<sup>224</sup> See CA2C Comments at 8 (citing Government Accountability Office (“GAO”), *Telecommunications: Direct Broadcast Satellite Subscribership Has Grown Rapidly, but Varies Across Different Types of Markets*, GAO-05-257 (April 2005)).

<sup>225</sup> See *id.* at 9.

<sup>226</sup> See DIRECTV Comments at 7-9 (quoting Judge Richard A. Posner as stating that “monopoly power” is “ordinarily inferred from possession of a dominant share (some courts set the threshold at 50 percent or occasionally even lower, others at 67 or even 70 percent) in a market sufficiently broadly defined to include all close substitutes of the defendant’s product” (citing Richard A. Posner, *Antitrust Law* 196 (2<sup>nd</sup> ed. 2001)); USTelecom Comments at 11.

<sup>227</sup> See DIRECTV Comments at 9-10; EchoStar Comments at 6.

<sup>228</sup> See AT&T Comments at 16; DIRECTV Comments at 10.

<sup>229</sup> See EchoStar Reply Comments at 4-5.

<sup>230</sup> See BSPA Comments at 17; CA2C Comments at 17-18; DIRECTV Comments at 10-11; RCN Comments at 7; Consumer Groups Reply Comments at 4-5; RCN Reply Comments at 10-11; SureWest Reply Comments at 3.

have acknowledged that clustering may enable cable operators to achieve greater economies of scale and scope, thereby reducing costs.<sup>231</sup>

48. Some competitive MVPDs argue that the recent entry of telephone companies into the video market provides cable operators with an increased incentive to withhold programming to stifle competition.<sup>232</sup> They contend that video service offered by telephone companies provides more price discipline to cable than does DBS and that telephone companies also offer broadband services in competition with cable operators.<sup>233</sup> They also note that wireline entry is still well below two percent of the nation's total MVPD subscribership.<sup>234</sup> AT&T and Verizon characterize as insignificant the short-term costs to cable incumbents of foregoing revenues from providing programming to the minimal subscriber bases of new entrants.<sup>235</sup> In the long term, they claim, the benefits to cable operators of limiting new entry will far outweigh the costs of lost revenues from excluding new entrants with minimal subscribership from their programming.<sup>236</sup> AT&T notes that the Commission in the *2002 Extension Order* found that cable operators had an economic incentive to withhold programming from DBS operators when the market share of DBS operators was 18 percent.<sup>237</sup> AT&T claims that the incentive for cable-affiliated programmers to withhold programming from new telephone company entrants with only a two percent market penetration is far greater.<sup>238</sup>

49. While cable MSOs argue that they have no incentive to withhold programming, competitive MVPDs provide the following examples which they claim demonstrate that cable MSOs will withhold programming if advantageous and permitted.<sup>239</sup> Competitive MVPDs argue that many of the examples listed below, involving terrestrially delivered programming (sports as well as non-sports) – for which the exclusive contract prohibition does not apply – demonstrate the incentive and ability of vertically integrated cable operators to deny access to programming where permitted by the statute.

<sup>231</sup> See Comcast Reply Comments at 14 n.41 (citing *Eighth Annual Report*, 17 FCC Rcd at 1304-05, ¶ 140; *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Seventh Annual Report, 16 FCC Rcd 6005, 6076, ¶ 166 (2001); *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Sixth Annual Report, 15 FCC Rcd 978, 1051, ¶¶ 161-62 (2000); *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Fifth Annual Report, 13 FCC Rcd 24284, 24371-72, ¶¶ 144-48 (1998); *Vertically Integrated Sports Programming: Are Cable Companies Excluding Competition? Before the Senate Comm. on the Judiciary*, 109<sup>th</sup> Cong. 4 (2006) (statement of Michael Salinger, Director, Bureau of Economics, FTC), available at: [http://judiciary.senate.gov/testimony.cfm?id=2454&wit\\_id=5929](http://judiciary.senate.gov/testimony.cfm?id=2454&wit_id=5929)).

<sup>232</sup> See AT&T Comments at 22-24; RCN Comments at 12; SureWest Reply Comments at 2; AT&T Reply Comments at 8-9.

<sup>233</sup> See AT&T Comments at 3, 22-23; USTelecom Comments at 6-7.

<sup>234</sup> See CA2C Comments at 5 (citing Letter from Daniel L. Brenner, Senior Vice President, Law & Regulatory Policy, National Cable & Telecommunications Association, MB Docket No. 92-264 (Mar. 16, 2007) at 4); Qwest Comments at 2-3; USTelecom Comments at 10-11.

<sup>235</sup> See AT&T Comments at 5; Verizon Comments at 12; RCN Reply Comments at 10.

<sup>236</sup> See AT&T Comments at 18-19.

<sup>237</sup> See AT&T Comments at 21 (citing *2002 Extension Order*, 17 FCC Rcd at 12144-45, ¶ 46).

<sup>238</sup> See *id.*

<sup>239</sup> See AT&T Comments at 4; BSPA Comments at 17; CA2C Comments at 17; RCN Comments at 10-11; RICA Comments at 5; SureWest Comments at 5-6; USTelecom Comments at 15-16; Verizon Comments at 12-14; CA2C Reply Comments at 7-8; EchoStar Reply Comments at 16-17; Qwest Reply Comments at 4; Verizon Reply Comments at 5-6.

*Sports Programming*

- *Comcast SportsNet Philadelphia.* Some competitive MVPDs state that Comcast refuses to make the terrestrially delivered Comcast SportsNet Philadelphia channel available to EchoStar and DIRECTV.<sup>240</sup> Competitive MVPDs cite the Commission's conclusion in the *Adelphia Order* that the percentage of households that subscribe to DBS service in Philadelphia is 40 percent below what would otherwise be expected.<sup>241</sup> In response, Comcast notes that Comcast SportsNet Philadelphia is available to RCN.<sup>242</sup>
- *Channel 4 San Diego.* Some competitive MVPDs claim that Cox makes available its Channel 4 San Diego network, which has exclusive rights to San Diego Padres baseball games, only to cable operators that do not directly compete with Cox and not to DIRECTV, EchoStar, and AT&T.<sup>243</sup> While competitive MVPDs state that DIRECTV's market penetration in San Diego is half of its national average,<sup>244</sup> Cablevision notes that DIRECTV in the *Adelphia* proceeding reported that it did not find a statistically significant effect on its market penetration in San Diego resulting from its inability to access this RSN.<sup>245</sup>
- *Overflow sports programming in New York, NY.* RCN notes that it was deprived of access to overflow sports programming from Cablevision after Cablevision revised its distribution system from satellite to terrestrial delivery.<sup>246</sup> While RCN filed a program access complaint, the Cable Services Bureau denied the complaint because the programming was terrestrially delivered and thus beyond the scope of Section 628(c)(2)(D).<sup>247</sup> The Bureau also found that Cablevision did not evade the Commission's rules by changing its distribution system from satellite to terrestrial delivery.<sup>248</sup>
- *RSNs Affiliated with Cablevision in New York and New England.* Verizon notes that it was forced to file a program access complaint against Cablevision and its vertically integrated programming subsidiary, Rainbow Media Holdings, LLC, in order to obtain access to RSNs in the New York City metropolitan area and New England.<sup>249</sup> While the dispute was eventually settled, competitive MVPDs state that the case illustrates the efforts of cable operators and their vertically integrated programmers to forestall competition from new entrants such as Verizon.<sup>250</sup>

<sup>240</sup> See CA2C Comments at 16; EchoStar Comments at 9; RCN Comments at 10; USTelecom Comments at 15.

<sup>241</sup> See AT&T Comments at 16 (citing *Adelphia Order*, 21 FCC Rcd at 8271, ¶ 149).

<sup>242</sup> See Comcast Reply Comments at 20.

<sup>243</sup> See AT&T Comments at 17; CA2C Comments at 16; USTelecom Comments at 15; Verizon Reply Comments at 5.

<sup>244</sup> See AT&T Comments at 17.

<sup>245</sup> See Cablevision Comments at 26 (citing *Adelphia Order*, 21 FCC Rcd at 8271, ¶ 148).

<sup>246</sup> See RCN Comments at 10; see also CA2C Comments at 17.

<sup>247</sup> See *RCN Telecom Services of New York, Inc. v. Cablevision Systems Corporation et al.*, 14 FCC Rcd 17093 (CSB, 1999), affirmed *RCN Telecom Services of New York, Inc. v. Cablevision Systems Corporation et al.*, 16 FCC Rcd 12048 (2001).

<sup>248</sup> See *id.*

<sup>249</sup> See Verizon Comments at 13.

<sup>250</sup> See AT&T Comments at 18; USTelecom Comments at 15; Verizon Comments at 13.



- *High Definition ("HD") Feeds of RSNs Affiliated with Cablevision.* While Rainbow has made available standard definition feeds of its RSNs, Verizon states that Rainbow is delivering HD feeds of this programming terrestrially to avoid the program access rules.<sup>251</sup> Verizon also claims that Cablevision's advertising campaign in New York City emphasizes its ability to offer more HD sports than its competitors.<sup>252</sup> In response, Comcast states that HD networks are distinct from their analog counterparts and that the Commission has recognized this distinction.<sup>253</sup>

#### *Non-Sports Programming*

- *New England Cable News ("NECN") in Boston, MA.* One commenter claims that RCN was provided with access to NECN, a terrestrially delivered network that is 50 percent owned by Comcast, only after the Senate Judiciary Committee indicated that they were considering legislative action to apply an exclusive contract prohibition to terrestrially delivered programming.<sup>254</sup>
- *PBS Kids Sprout.* AT&T and RCN claim that after PBS Kids Sprout became vertically integrated with Comcast, RCN lost access to the network, resulting in an 83 percent drop in the usage of its children's VOD service.<sup>255</sup> Comcast and PBS Kids Sprout dispute these allegations, stating that this programming is available to all MVPDs and, in fact, RCN, Verizon, and AT&T currently distribute PBS Kids Sprout.<sup>256</sup>
- *iN DEMAND.* CA2C notes that iN DEMAND is jointly owned by Time Warner, Comcast, and Cox.<sup>257</sup> CA2C argues that iN DEMAND has taken the position that its programming is beyond the scope of the exclusive contract prohibition in Section 628(c)(2)(D) because iN DEMAND programming is delivered to MVPDs terrestrially.<sup>258</sup> CA2C claims that iN DEMAND initially refused to provide its service to BSPs that competed with incumbent cable operators and that it reversed this position only after meetings were held with the Antitrust Subcommittee of the Senate Judiciary Committee.<sup>259</sup> Nonetheless, CA2C contends that iN DEMAND has refused to provide its service to Hiawatha Broadband because of the technology Hiawatha uses for its distribution system.<sup>260</sup> Qwest provides a declaration regarding its alleged inability to acquire iN DEMAND's sports packages in a timely manner.<sup>261</sup>

<sup>251</sup> See Verizon Comments at 13-14; Verizon Reply Comments at 5.

<sup>252</sup> See Verizon Comments at 13.

<sup>253</sup> See Comcast Reply Comments at 29 n.90 (citing 12<sup>th</sup> Annual Report, 21 FCC Rcd at 2626-42, Table C-2).

<sup>254</sup> See CA2C Comments at 16-17.

<sup>255</sup> AT&T Comments at 15; RCN Reply Comments at 7.

<sup>256</sup> See Comcast Reply Comments at 21; Letter from Sandy Wax, President, and Adrienne Byrd, Senior Director, Legal Affairs, PBS KIDS Sprout, to Ms. Marlene H. Dortch, FCC, MB Docket No. 07-29 (May 3, 2007).

<sup>257</sup> See CA2C Reply Comments at 7.

<sup>258</sup> See *id.*

<sup>259</sup> See *id.* at 7-8.

<sup>260</sup> See *id.* at 8.

<sup>261</sup> See Qwest Reply Comments at 4; *see also* CA2C Reply Comments at 8.

- *CN8 – The Comcast Network*. Qwest claims that CN8 – The Comcast Network is a local news and information channel that serves 12 states and 20 television markets but is only available to Comcast and Cablevision subscribers because it is terrestrially delivered and therefore beyond the scope of Section 628(c)(2)(D).<sup>262</sup>
- *NRTC*. NRTC, which acts as a “buying group” on behalf of its members, claims that it has been denied access to two vertically integrated programming networks, the identities of which it claims it cannot disclose due to non-disclosure agreements.<sup>263</sup>

AT&T argues that if cable-affiliated programmers had an economic incentive to distribute their programming as widely as possible, as cable MSOs claim, then there would be no examples of any such exclusionary behavior.<sup>264</sup> AT&T also notes that cable operators actively advertise their exclusive access to certain content in order to attract and retain subscribers.<sup>265</sup> Comcast contends these examples do not offer sufficient proof of market failure that requires government intervention.<sup>266</sup>

50. *Discussion*. We conclude that vertically integrated cable programmers retain the incentive to withhold programming from their competitors. We recognize the pro-competitive developments in the MVPD market since the *2002 Extension Order*, such as the reduction in the cable industry’s share of MVPD subscribers from 78 percent to an estimated 67 percent and the increase in the DBS industry’s market share from 18 percent to approximately 30 percent.<sup>267</sup> Despite these positive trends, however, almost seven out of ten subscribers still choose cable over competitive MVPDs, the percentage of all MVPD subscribers nationwide served by one of the four largest vertically integrated cable operators has increased substantially since 2002, and cable operators have continued to raise prices in excess of inflation.<sup>268</sup> While cable MSOs claim that the emergence of telephone companies as new video competitors demonstrates that competition is flourishing, the fact is that, based on estimates provided by the cable industry, competitive MVPDs, excluding DBS operators, serve approximately three percent of all MVPD subscribers nationwide, which accounts for less than three million total MVPD subscribers.<sup>269</sup> Moreover, as we explained in our decision on franchising reform, competition from cable overbuilders is minimal, with only a few hundred examples of competitive franchises throughout the nation.<sup>270</sup> This is one reason why we have explored ways to lower barriers to entry in the video

<sup>262</sup> See Qwest Comments at 4.

<sup>263</sup> See NRTC Comments at 5.

<sup>264</sup> See AT&T Comments at 19.

<sup>265</sup> See *id.* at 19-20; AT&T Reply Comments at 4.

<sup>266</sup> See Comcast Reply Comments at 19.

<sup>267</sup> See *supra* note 100 (indicating that DBS operators have an approximate 30 percent share of the MVPD market).

<sup>268</sup> See *2006 Cable Price Report*, 21 FCC Rcd at 15087-88, ¶ 2.

<sup>269</sup> See *supra* note 96 (indicating that cable operators have an approximate 67 percent share of the MVPD market); *supra* note 100 (indicating that DBS operators have an approximate 30 percent share of the MVPD market); USTelecom Comments at 10 (citing *12<sup>th</sup> Annual Report*, 21 FCC Rcd at 2506-07, ¶ 8 (stating that, as of June 2005, only 2.9 percent of MVPD subscribers receive service from an alternative provider to cable or DBS)); see also CA2C Comments at 5 (“Despite the growth of DBS, cable operators have still maintained their position in the market.”); USTelecom Comments at 9 (“Now, nearly five years since the [*2002 Extension Order*], the MSOs’ grip on the multichannel video market has remained firm . . .”).

<sup>270</sup> See *Local Franchising Report and Order*, 22 FCC Rcd at 5110, ¶ 19.

marketplace.<sup>271</sup> Although we are encouraged by developments since 2002, we do not believe these developments have been significant enough for us to reverse the Commission's previous conclusion that cable operators have market dominance of sufficient magnitude that, in the absence of the prohibition, they would be able to act in an anticompetitive manner.<sup>272</sup>

51. We also conclude that cable-affiliated programmers continue to have an economic incentive to favor their affiliated cable operators over competitive MVPDs by entering into exclusive agreements. We agree that in many instances a cable-affiliated programmer may choose to provide its programming to as many platforms as possible in order to maximize advertising and subscription revenues. In other cases, however, cable-affiliated programmers will have an incentive to withhold programming from competitive MVPDs in order to favor their affiliated cable operator. Our conclusion that vertically integrated cable programmers retain the incentive to withhold programming from their competitors is reinforced by specific factual evidence that vertically integrated programmers have withheld and continue to withhold programming, including both sports and non-sports programming, from competitive MVPDs.<sup>273</sup> While many of these examples pertain to terrestrially delivered programming that is beyond the scope of Section 628(c)(2)(D), we find that these examples are nonetheless significant because they demonstrate that, absent a prohibition, cable-affiliated programmers will engage in withholding of programming from competitive MVPDs. Moreover, because it is outside of the scope of the program access provisions, the withholding of terrestrially delivered programming presents the most direct, factually based evidence of cable MSO behavior if the prohibition is permitted to lapse. If vertically integrated programmers had no economic incentive other than to distribute their programming to as many platforms as possible, then we would not expect to see such examples of withholding.<sup>274</sup>

52. While the cable industry's share of MVPD subscribers nationwide has decreased from 78 percent to approximately 67 percent since the *2002 Extension Order*,<sup>275</sup> we conclude that this market share is still sufficient to enable cable-affiliated programmers to make withholding vertically integrated programming a profitable strategy. Moreover, while the cable industry's share of MVPD subscribers nationwide has declined since the *2002 Extension Order*, it has remained above or near the 78 percent

<sup>271</sup> See *id.* at 5111, ¶ 20; *MDU Access NPRM*, 22 FCC Rcd at 5938, ¶ 6.

<sup>272</sup> See *2002 Extension Order*, 17 FCC Rcd at 12143-45, ¶¶ 45-46.

<sup>273</sup> See *supra* ¶ 49 (discussing evidence of withholding of cable-affiliated programming from competitive MVPDs); *DIRECTV, Inc. v. Comcast Corporation*, 15 FCC Rcd 22802, 22807-08, ¶¶ 11-14 (2000) (resolving program access dispute), *aff'd*, *EchoStar Communications Corporation v. Comcast Corporation*, 14 FCC Rcd 2089 (1999), *DIRECTV, Inc. v. Comcast Corporation*, 13 FCC Rcd 21822 (1998), *aff'd sub nom. EchoStar Communications Corporation v. FCC*, 292 F.3d 749 (D.C. Cir. 2002); *RCN Telecom Services of New York, Inc. v. Cablevision Systems Corporation et al.*, 14 FCC Rcd at 17103-07, ¶¶ 20-27 (resolving program access dispute), *affirmed RCN Telecom Services of New York, Inc. v. Cablevision Systems Corporation et al.*, 16 FCC Rcd 12048 (2001); see also *EchoStar Comments* at 9 ("Indeed, cable conglomerates have already demonstrated their willingness to abuse exclusive programming rights to gain market share and harm consumers. The well-worn example of Comcast's conduct in Philadelphia with its SportsNet asset is again instructive.").

<sup>274</sup> While cable MSOs claim that competitive MVPDs were unable to demonstrate any harm to their ability to compete in one of these cases (*Channel 4 San Diego*) (see *Cablevision Comments* at 26 (citing *Adelphia Order*, 21 FCC Rcd at 8271, ¶ 148)), this is irrelevant to the issue of whether cable-affiliated programmers have the incentive to engage in withholding of programming from competitive MVPDs. These examples demonstrate that, absent a prohibition, cable-affiliated programmers have an incentive to engage in withholding.

<sup>275</sup> See *supra* note 96 (indicating that cable operators have an approximate 67 percent share of the MVPD market).

level in many Designated Market Areas ("DMAs"),<sup>276</sup> indicating that cable operators retain the same share of MVPD subscribers in many markets as in 2002.<sup>277</sup> In the 2002 *Extension Order*, based on the cable industry's 78 percent national market share at the time, the Commission found that a "cable-only" distribution strategy would reduce potential subscribership or viewership for a cable-affiliated programming network by one-fifth.<sup>278</sup> The Commission concluded that the revenues foregone by a cable-affiliated programmer by refusing to sell to competitive MVPDs would thus be "relatively low."<sup>279</sup> While the reduction in potential nationwide subscribership or viewership has now increased to one-third based on the cable industry's current national market share of approximately 67 percent, we find that this reduction in potential subscribership or viewership has not reached a point where withholding would be unprofitable.<sup>280</sup> Moreover, because the share of MVPD subscribers held by cable operators is above or near 78 percent in many DMAs, there is no reduction in potential subscribership or viewership in many regional areas from that which we observed in the 2002 *Extension Order*.<sup>281</sup> As the Commission did in the 2002 *Extension Order*, we find that the costs (i.e., foregone revenues) incurred by a cable-affiliated programmer by refusing to sell to competitive MVPDs would be offset by (i) revenues from increased subscriptions to the services of its affiliated cable operator resulting from subscribers that switch to cable to obtain access to the cable-exclusive programming,<sup>282</sup> (ii) revenues from increased rates charged by the

<sup>276</sup> A DMA is a geographic market designation that defines each television market exclusive of others, based on measured viewing patterns. Each county in the United States is allocated to a market based on which home-market stations receive a preponderance of total viewing hours in the county. For purposes of this calculation, both over-the-air and cable television viewing are included. See *Time Warner Entertainment*, Memorandum Opinion and Order, DA 07-3400, 2007 WL 2159623, ¶ 2 (MB, 2007).

<sup>277</sup> See 2002 *Extension Order*, 17 FCC Rcd at 12132-33, ¶ 20 (citing 8<sup>th</sup> Annual Report, 17 FCC Rcd at 1247, ¶ 5). Based on data from Nielsen Media Research, as of July 2007, the share of MVPD subscribers held by cable operators exceeds 78 percent in 36 out of 210 DMAs and is between 75 and 78 percent in an additional 16 DMAs. See DMA Household Universe Estimates July 2007: Cable And/Or ADS (Alternate Delivery Systems), [http://www.tvb.org/nav/build\\_frameset.asp](http://www.tvb.org/nav/build_frameset.asp) (follow "Research Central" hyperlink; then follow "Market Track" hyperlink; then follow "Cable and ADS Penetration by DMA" hyperlink) (last visited Aug. 2, 2007). These include sixteen of the Top 50 most-populated DMAs: New York (No. 1; 83.7 percent cable market share); Philadelphia (No. 4; 81.1 percent cable market share); Boston (No. 7; 87.1 percent cable market share); Tampa-St. Pete (No. 12; 81.1 percent cable market share); Seattle (No. 14; 79.3 percent cable market share); Cleveland-Akron (No. 17; 78.6 percent cable market share); Orlando (No. 19; 75.7 percent cable market share); Pittsburgh (No. 22; 79.6 percent cable market share); Baltimore (No. 24; 80.3 percent cable market share); San Diego (No. 27; 87.1 percent cable market share); Hartford-New Haven, CT (No. 28; 86.4 percent cable market share); Columbus (No. 32; 78 percent cable market share); Milwaukee (No. 34; 79.1 percent cable market share); Harrisburg-Lancaster, PA (No. 41; 79.5 percent cable market share); Norfolk-Portsmouth-Newport News, VA (No. 42; 77.6 percent cable market share); Las Vegas (No. 43; 75.9 percent cable market share). See *id.*

<sup>278</sup> See 2002 *Extension Order*, 17 FCC Rcd at 12147-48, ¶ 53.

<sup>279</sup> See *id.*

<sup>280</sup> We also noted in the 2002 *Extension Order* that if vertically integrated programmers entered into exclusive arrangements with only the top ten MVPDs (excluding DBS providers), those programmers would still retain access to over 66 percent of all MVPD subscribers, which reflected a three percent increase from 1994. See 2002 *Extension Order*, 17 FCC Rcd at 12148, ¶ 53 n.172. These figures are similar in the current video distribution market. Today, if vertically integrated programmers entered into exclusive arrangements with only the top ten MVPDs (excluding DBS providers), those programmers would still retain access to over 60 percent of all MVPD subscribers. See 12<sup>th</sup> Annual Report, 21 FCC Rcd at 2620, Table B-3.

<sup>281</sup> See 2002 *Extension Order*, 17 FCC Rcd at 12147-48, ¶ 53.

<sup>282</sup> See *id.*

affiliated cable operator in response to increased demand for its services resulting from its ability to offer exclusive programming;<sup>283</sup> and (iii) revenues resulting from the ability of the cable-affiliated programmer to raise the price it charges for programming to other cable operators in return for exclusivity.<sup>284</sup> Thus, particularly where competitive MVPDs are limited in their market share, a cable-affiliated programmer will be able to recoup a substantial amount, if not all, of the revenues foregone by pursuing a withholding strategy. In the long term, a withholding strategy may result in a reduction in competition in the video distribution market, thereby allowing the affiliated cable operator to raise rates. As discussed in Appendix C, we have also made critical value calculations which conclude that withholding of some nationally distributed programming networks could be profitable if as little as 1.9 percent of non-cable subscribers were to switch to cable as a result of the withholding.<sup>285</sup> We believe that these subscriber numbers are sufficiently low as to make it likely that cable MSOs will pursue national "cable only" withholding strategies with some networks in the absence of the exclusivity prohibition. We thus conclude that the one-third share of the MVPD market held by competitive MVPDs remains limited enough to allow cable-affiliated programmers to successfully and profitably implement a withholding strategy.

53. We also find that three additional developments since 2002 provide cable-affiliated programmers with an even greater economic incentive to withhold programming from competitive MVPDs: (i) the increase in horizontal consolidation in the cable industry; (ii) the increase in clustering of cable systems; and (iii) the recent emergence of new entrants in the video market place, such as telephone companies.

54. *Horizontal Consolidation.* The cable industry has continued to consolidate since 2002. Since this time, the percentage of MVPD subscribers receiving their video programming from one of the four largest vertically integrated cable MSOs (Comcast, Time Warner, Cox, and Cablevision) has increased from 34 percent<sup>286</sup> to between 54 and 56.75 percent.<sup>287</sup> Moreover, the percentage of MVPD subscribers receiving their video programming from one of the four largest cable MSOs (Comcast, Time Warner, Cox, and Charter) has increased from 48 percent<sup>288</sup> to between 53 and 60 percent after taking into account the recent acquisition by Comcast and Time Warner of cable systems formerly owned by Adelphia.<sup>289</sup> Thus, while the evidence demonstrates that the market share of small-to-medium sized, non-vertically integrated cable operators has declined, the market share of large cable operators, and in particular those that own cable programming, has increased substantially since 2002. In the 2002 *Extension Order*, the Commission observed that because four of the five largest vertically integrated cable operators served 34 percent of all MVPD subscribers, they could reap a substantial portion of the gains from withholding programming from their rivals.<sup>290</sup> Now that the market share of the four largest

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<sup>283</sup> See *id.*

<sup>284</sup> See *id.*

<sup>285</sup> See Appendix C, ¶ 21.

<sup>286</sup> See 2002 *Extension Order*, 17 FCC Rcd at 12133, ¶ 20 (citing 8<sup>th</sup> *Annual Report*, 17 FCC Rcd at 1341, Table C-3).

<sup>287</sup> See *supra* note 131 (discussing percentage of MVPD subscribers receiving their video programming from one of the four largest vertically integrated cable MSOs).

<sup>288</sup> See 2002 *Extension Order*, 17 FCC Rcd at 12133, ¶ 21.

<sup>289</sup> See *supra* note 129 (discussing percentage of MVPD subscribers receiving their video programming from one of the four largest cable operators).

<sup>290</sup> See 2002 *Extension Order*, 17 FCC Rcd at 12147-48, ¶ 53.

vertically integrated cable MSOs has increased to between 54 and 56.75 percent, the largest vertically integrated cable operators stand to gain even more from a withholding strategy.<sup>291</sup> Thus, the increase in horizontal consolidation in the cable industry since 2002 increases the incentive to pursue anticompetitive withholding strategies.

55. *Clustering.* The cable industry has continued to form regional clusters since the 2002 *Extension Order*, when approximately 80 percent of cable subscribers were served by systems that were part of regional clusters.<sup>292</sup> Today, taking into account the sale of Adelphia's systems to Comcast and Time Warner, some estimate that the percentage of cable subscribers served by systems that are part of regional clusters has increased to between 85 and 90 percent.<sup>293</sup> The Commission concluded in the 2002 *Extension Order* that horizontal consolidation and clustering combined with affiliation with regional programming contributed to the cable industry's overall market dominance.<sup>294</sup> Given the increase in horizontal consolidation and regional clustering since 2002, this statement is no less true today. With a regional programming denial strategy, a cable-affiliated programmer foregoes only those revenues associated with the subscribers of competitive MVPDs within the cluster, not the revenues associated with subscribers of competitive MVPDs nationwide.<sup>295</sup> As the Commission concluded previously, in many cities where cable MSOs have clusters, the market penetration of competitive MVPDs is much lower and cable market penetration is much higher than their nationwide penetration rates.<sup>296</sup> Moreover, due to the national distribution of DBS services and the insufficient mass of DBS subscribers on a regional basis, DBS operators do not have an economic base for substantial regional programming investments on a market-by-market basis.<sup>297</sup> As a result, the cost to a cable-affiliated programmer of withholding regional programming is lower in many cases than the cost of withholding national programming. Moreover, the affiliated cable operator will obtain a substantial share of the benefits of a withholding strategy because its share of subscribers within the cluster is likely to be inordinately high.<sup>298</sup> While Comcast claims that increased clustering may result in synergies and cost-saving efficiencies, this

<sup>291</sup> See EchoStar Comments at 2-6; USTelecom Comments at 9-10; see also *supra* note 131 (discussing percentage of MVPD subscribers receiving their video programming from one of the four largest vertically integrated cable MSOs).

<sup>292</sup> See 2002 *Extension Order*, 17 FCC Rcd at 12133-34, ¶ 22 (citing 8<sup>th</sup> *Annual Report*, 17 FCC Rcd at 1252, ¶ 14).

<sup>293</sup> See *Consumer Groups Reply* at 4-5.

<sup>294</sup> See 2002 *Extension Order*, 17 FCC Rcd at 12125, ¶ 4.

<sup>295</sup> See *id.* at 12148-49, ¶ 54.

<sup>296</sup> See *id.* For example, according to data from Nielsen Media Research, the collective market penetration of competitive MVPDs in many DMAs where cable MSOs have clusters is far less than their collective nationwide market penetration rate (approximately 33 percent): San Diego (13.7 percent), New York (18.2 percent), Philadelphia (19.8 percent), and San Francisco (26.9 percent). See DMA Household Universe Estimates July 2007: Cable And/OR ADS (Alternate Delivery Systems), [http://www.tvb.org/nav/build\\_frameset.asp](http://www.tvb.org/nav/build_frameset.asp) (follow "Research Central" hyperlink; then follow "Market Track" hyperlink; then follow "Cable and ADS Penetration by DMA" hyperlink) (last visited Aug. 2, 2007). As the Commission acknowledged in the 2002 *Extension Order*, this market penetration data may not correspond exactly to cable MSO cluster boundaries, and there are likely other factors, such as line-of-sight, in addition to cable competition that affect city market penetration. See 2002 *Extension Order*, 17 FCC Rcd at 12148-49, ¶ 54 n.177. Nevertheless, we believe that this market penetration data provide support for the position that market penetration of competitive MVPDs is lower in certain cable cluster areas than nationwide. See *id.*

<sup>297</sup> See 2002 *Extension Order*, 17 FCC Rcd at 12151, ¶ 59.

<sup>298</sup> See *id.*

has no relevance to the issue of the impact of increased clustering on the potential for regional programming denial strategies.<sup>299</sup>

56. As discussed further in Appendix C, although cable's national share of total MVPD subscribers has declined, the situation is somewhat different at the individual market level. In some markets, the cable share of MVPD subscribers remains high, well above the average level and, indeed, above the 2002 national level of 78 percent that we found problematic in the *2002 Extension Order*.<sup>300</sup> However, clustering -- an increase over time in the number of cable subscribers and homes passed by a single MSO in particular markets (accomplished via internal growth as well as by acquisitions) -- also enhances the potential profitability of withholding regional programming from rivals. To understand the impact of this development in the cable television sector, we consider the calculations of a vertically integrated satellite cable programmer ("VISCP") that is contemplating a "cable-only" strategy of withholding its RSN from DBS and other non-cable MVPDs in the market. If the RSN is withheld, the VISCP will lose, initially, all those subscribers who were receiving the RSN via non-cable MVPDs. Some of those subscribers will switch to cable in order to retain access to the RSN. Of course, only those subscribers whose homes are passed by cable have the option to switch. Thus, the share of television households in the market that are passed by cable, either the VISCP's cable affiliate or other operators, is of importance. With respect to those subscribers that switch to a cable operator other than the VISCP's cable affiliate, the VISCP will simply regain the revenues (affiliation fee and network advertising revenue per subscriber) lost due to withholding from the non-cable MVPDs. However, with respect to those who switch to the VISCP's cable affiliate, the VISCP will gain substantially more. Those who switch to the VISCP's cable affiliate do not simply purchase the RSN. Rather, they must purchase a full video package from the VISCP's cable affiliate. Thus, the VISCP and its cable affiliate gain the full additional profit from a new subscriber, in addition to regaining the network advertising revenue per subscriber lost temporarily due to the withholding.<sup>301</sup> The key point is that the larger the share of television households in the market that is served by the VISCP's cable affiliate (*i.e.*, the larger the ratio of homes passed by the VISCP's cable affiliate to total television households), the larger is the total number of switching subscribers that switch to the VISCP's cable affiliate (as opposed to switching to another cable operator), and the greater is the potential compensating gain to the VISCP and its cable affiliate.

57. Thus, separate from what has been occurring in the national MVPD market, certain developments in the cable market may have made withholding of regional networks potentially more profitable than previously. Two types of empirical analyses can be performed to assess these developments. First, it is possible to track changes in clustering from 2002 to 2007 for certain key MSOs. Second, it is possible, under certain simplifying assumptions, to assess the circumstances under which withholding of regional programming would be profitable in the absence of the exclusivity restriction.<sup>302</sup>

<sup>299</sup> See Comcast Reply Comments at 13-14.

<sup>300</sup> Nielsen Media Research data for May 2007 indicate that there are 40 DMAs with a wired cable percentage of total subscription television households greater than 78 percent. The 40 comprise: 13 in the top 50 markets, another 8 in the top 100 markets, and 19 in markets above 100. Of the 14 markets with shares between 75 and 78 percent, there are 4 in the top 50, another 5 in the top 100, and 5 above 100. See DMA Household Universe Estimates May 2007: Cable And/Or ADS (Alternate Delivery Systems), [http://www.tvb.org/nav/build\\_frameset.asp](http://www.tvb.org/nav/build_frameset.asp) (follow "Research Central" hyperlink; then follow "Market Track" hyperlink; then follow "Cable and ADS Penetration by DMA" hyperlink; then follow "ADS Archives" hyperlink) (last visited Aug. 2, 2007).

<sup>301</sup> There is no gain in affiliation fee, since the VISCP is paying that to its affiliate for its own subscribers.

<sup>302</sup> *Hughes Order*. 19 FCC Rcd at 633-48, Appendix D (explaining methodology).

58. *Analysis of Increase in Clustering from 2002 to 2007.* Substantial increases in clustering, i.e., the number of DMAs in which homes passed by a single cable operator is a large share of total television households, would mean that withholding is likely more profitable than it was before. This calculus (assuming the market structure and financial parameters stated in Appendix C) applies not only to markets where there is a VISCP, but to any market, since, if the exclusivity limit were relaxed, any cable operator would be permitted to start a new regional network or acquire an existing one and then withhold it from rivals. As discussed in Appendix C, we conclude that there has been a substantial increase in clustering among the two largest vertically integrated cable operators since adoption of the 2002 Extension Order.

59. *Analysis of Profitability of Withholding of Regional Programming.* The second type of analysis we conducted was to estimate directly the profitability of withholding a regional network based on the structure of the market<sup>303</sup> and certain financial parameters.<sup>304</sup> These calculations were made for all DMAs for which data were available, using Comcast and Time Warner subscriber and profitability estimates from public sources, and using 2006 data on the average affiliate fee and network advertising revenue per subscriber for an RSN. The analysis yields a "critical value," representing the percentage of current non-cable MVPD subscribers in a DMA that would need to switch to cable in response to withholding of an RSN in order to make this strategy profitable. In order to determine what critical value is realistic, we examined the case of Philadelphia, where Comcast is currently withholding its RSN from DBS operators. As explained in Appendix C, withholding in the Philadelphia DMA of an RSN with average profile would be profitable if 5.45 to 8.4 percent of non-cable MVPD subscribers switched to cable. Conducting the analysis using the actual 2006 profile of the Comcast SportsNet Philadelphia RSN yields critical values in the 6.81 to 10.49 percent range. As explained in detail in Appendix C, the data demonstrates that (i) withholding would be profitable for Comcast in as many as 39 DMAs;<sup>305</sup> and (ii) withholding would be profitable for Time Warner in as many as 20 DMAs.<sup>306</sup> The calculations further demonstrate that, using Comcast profitability figures and the Comcast SportsNet Philadelphia RSN profile, withholding becomes profitable when a single MSO reaches homes passing roughly 60 percent of television households in a DMA. Using Time Warner profitability and the Comcast SportsNet Philadelphia RSN profile, withholding would become profitable when a single MSO reaches homes passing at least 80 percent of television households in a DMA. Our assessment of the calculated critical values convinces us that, in a significant range of cases, withholding of an RSN would be profitable for the VISCP and that, absent the exclusivity prohibition, valuable programming would be withheld from rival MVPDs.

60. *Recent Entrants.* Another significant development since 2002 is the emergence of new entrants into the video marketplace, including telephone companies.<sup>307</sup> We agree that vertically integrated

<sup>303</sup> Factors considered include: the share of television households in the market passed by a VISCP's cable affiliate; the share of television households in the market passed by other cable operators; and the share of television households in the market that subscribe to a non-cable MVPD.

<sup>304</sup> Factors considered include: per subscriber profits (net of amortized subscriber acquisition cost) earned per month by the VISCP's cable affiliate on a new cable subscriber; affiliate fee revenue per subscriber earned by the VISCP from its regional network; and network advertising revenue per subscriber earned by the VISCP from its regional network.

<sup>305</sup> The data indicates that Comcast provides service to at least part of 97 DMAs.

<sup>306</sup> The data indicates that Time Warner provides service to at least part of 89 DMAs.

<sup>307</sup> At the time of the 2002 Extension Order, competition in the video marketplace from telephone companies had not yet emerged. Indeed, we stated at the time that "the strong overbuild competition from local exchange carriers (continued....)"



cable programmers may have an even greater economic incentive to withhold programming from these recent entrants in the video marketplace. Because recent entrants have minimal subscriber bases at this time, the costs that a cable-affiliated programmer would incur from withholding programming from recent entrants are negligible.<sup>308</sup> To be sure, a vertically integrated programmer that withholds programming from one competitive MVPD in a market would generally need to withhold the programming from all other competitive MVPDs in the market, thereby increasing the foregone revenues resulting from a withholding strategy.<sup>309</sup> Even so, the short term costs to the vertically integrated programmer of withholding its programming from all competitive MVPDs (*i.e.*, the reduction in potential advertising or subscription revenues) are likely to be outweighed by the long term benefits to its affiliated cable operator of (i) hindering and potentially eliminating competition from new entrants, including those with substantial resources such as incumbent telephone companies; and (ii) increased revenues resulting from attracting subscribers away from competitive MVPDs. Cable MSOs suggest that if the justification for extending the exclusive contract prohibition is the emergence of new competitors, then the exclusive contract prohibition could be extended in perpetuity whenever new potential competitors emerge.<sup>310</sup> We disagree. As discussed above, vertically integrated programmers are likely to have the incentive to withhold programming only when their affiliated cable operators have a sufficient share of the distribution market to minimize the impact of foregone subscription and advertising revenues from denying access to other distributors. At this time, we conclude that vertically integrated programmers are likely to retain this incentive given the 67 percent share of the video distribution market held by cable operators. If competition in the MVPD market continues to develop and cable market share continues to decline, however, the incentive of vertically integrated programmers to engage in withholding will presumably diminish to the extent that we may be able to relax the exclusive contract prohibition. Moreover, the availability of exclusivity petitions pursuant to Section 628(c)(2) and (4) allows for appropriate treatment of unique competitive situations.

61. Cable MSOs argue that new entrants in the video marketplace such as AT&T and Verizon will never exit the video distribution market regardless of whether they are denied access to cable-affiliated programming because of the substantial sunk investments they have already made in video distribution networks.<sup>311</sup> In considering whether to allow the exclusive contract prohibition to sunset, our primary focus is on the impact that sunset would have on competition and diversity in the distribution of video programming generally, not on individual competitors and not on programming

(Continued from previous page)

and others that Congress anticipated as a result of the 1996 amendments to the Communications Act has, as yet, failed to develop.” *See 2002 Extension Order*, 17 FCC Rcd at 12144-45, ¶ 46.

<sup>308</sup> *See* AT&T Comments at 5; Verizon Comments at 12; AT&T Reply Comments at 8-9; RCN Reply Comments at 10.

<sup>309</sup> We note that, if the exclusive contract prohibition in Section 628(c)(2)(D) were to sunset, other program access provisions in Section 628 would remain, including the prohibition on discrimination. *See* 47 U.S.C. § 628(c)(2)(B); 47 C.F.R. § 76.1002(b). Thus, a vertically integrated programmer that withholds programming from a recent entrant with a minimal subscriber base but chooses to offer the programming to all other competitive MVPDs in the market could be found in violation of the program access rules based on an unreasonable refusal to sell. *See First Report and Order*, 8 FCC Rcd at 3412-13, ¶ 116 (stating that non-price discrimination could include a vendor’s refusing to initiate discussions with a particular distributor when the vendor has sold its programming to that distributor’s competitor). As discussed below, while other program access provisions in Section 628 would remain if Section 628(c)(2)(D) were to sunset, we find that these other provisions are insufficient to preserve and protect competition at this time. *See infra* n. 320.

<sup>310</sup> *See* NCTA Reply Comments 2, 4; *see also* Comcast Comments at 5 n.5.

<sup>311</sup> *See* Cablevision Comments at 15-16; Cablevision Reply Comments at 11; Time Warner Reply Comments at 21.

diversity.<sup>312</sup> Thus, the more salient point for our analysis is not whether individual competitors will remain in the market if the exclusive contract prohibition were to sunset, but how competition in the video distribution market will be impacted if the exclusive contract prohibition were to sunset. We find that absent the exclusive contract prohibition, the ability of competitive MVPDs, including large and established companies, to compete will be severely hindered, thereby adversely impacting the market for distribution of video services.<sup>313</sup> Cablevision argues that a competitive MVPD could engage in competitive countermeasures in reaction to a cable-affiliated programmer's decision to withhold "must have" programming, such as lowering prices, acquiring other programming on an exclusive basis, or launching new services of its own.<sup>314</sup> We find, however, that these countermeasures would not be sufficient to deprive cable-affiliated programmers of the incentive to withhold programming or to mitigate the impact to the competitive MVPD of being unable to offer subscribers essential programming. The record reflects that, despite the availability of these countermeasures, cable-affiliated programmers have withheld programming from competitive MVPDs and in two instances – San Diego and Philadelphia – that such withholding has had a material adverse impact on competition in the video distribution market.<sup>315</sup> As the Commission concluded in the 2002 *Sunset Order*, the prohibition on exclusivity therefore remains necessary to preserve and protect diversity in distribution of video programming.

62. We disagree with cable MSOs that argue that enforcement of antitrust laws will be sufficient to address anticompetitive use of exclusive contracts.<sup>316</sup> In passing the exclusive contract prohibition in Section 628(c)(2)(D), Congress concluded the opposite by requiring the Commission to enforce a presumptive ban on exclusive contracts rather than relying on reactive application of antitrust laws to existing exclusive arrangements.<sup>317</sup> Moreover, the legislative history of the 1992 Cable Act reflects Congress's concern regarding the "prohibitive cost of pursuing an antitrust suit."<sup>318</sup> As the Commission emphasized in the 2002 *Extension Order*, "Congress already determined that antitrust laws were not a viable alternative for achieving the government's goals in this instance."<sup>319</sup> As discussed above, we do not believe that Congress's goal of achieving competition and diversity in the video distribution marketplace has been achieved. Accordingly, we believe that continued reliance on the exclusive contract prohibition in Section 628(c)(2)(D) rather than reliance solely on antitrust laws better serves the intent of Congress.<sup>320</sup>

<sup>312</sup> 47 U.S.C. § 548(c)(2)(D); see 2002 *Extension Order*, 17 FCC Rcd at 12150, ¶ 58 and 12152, ¶ 62; see *infra* Section III.A.3.c.

<sup>313</sup> See 2002 *Extension Order*, 17 FCC Rcd at 12152-53, ¶ 63.

<sup>314</sup> See Cablevision Comments at 8, 17; Cablevision Reply Comments at 11-12.

<sup>315</sup> See *supra* ¶ 39 (discussing impact on competitive MVPD subscribership from withholding of cable-affiliated programming) and ¶ 49 (discussing evidence of withholding of cable-affiliated programming from competitive MVPDs).

<sup>316</sup> See Comcast Comments at 23-24; Comcast Reply Comments at 22.

<sup>317</sup> See CA2C Reply Comments at 3; EchoStar Reply Comments at 15-16; Qwest Reply Comments at 7 n.22; Verizon Reply Comments at 6. EchoStar notes that antitrust enforcement is slow, time-consuming, and provides no means to check anticompetitive behavior prospectively, other than through a stay. EchoStar Reply Comments at 15.

<sup>318</sup> S. Rep. No. 102-92, at 29 (1991), reprinted in 1992 U.S.C.C.A.N. 1133, 1162.

<sup>319</sup> See 2002 *Extension Order*, 17 FCC Rcd at 12143, ¶ 45 n.138.

<sup>320</sup> As we concluded in the 2002 *Extension Order*, Sections 628(b), 628(c)(2)(A), and 628(c)(2)(B) of the Communications Act are not adequate substitutes for the particularized protection afforded under Section (continued....)

63. We recognize the benefits of exclusive contracts and vertical integration cited by some cable MSOs, such as encouraging innovation and investment in programming and allowing for “product differentiation” among distributors.<sup>321</sup> We do not believe, however, that these purported benefits outweigh the harm to competition and diversity in the video distribution marketplace that would result if we were to lift the exclusive contract prohibition. In addition, the Commission’s rules permit cable-affiliated programmers to seek approval to enter into an exclusive contract based on a demonstration that the exclusive arrangement serves the public interest consistent with factors established by Congress.<sup>322</sup> Despite the option to seek approval to enter into exclusive contracts, only ten exclusivity petitions have been filed in the fifteen years since enactment of Section 628(c)(2)(D) in the 1992 Cable Act. Of these petitions, two were granted,<sup>323</sup> three were denied,<sup>324</sup> and five were dismissed at the request of the parties. Of the three exclusivity petitions that have been denied, all of the networks that were the subject of these petitions (Court TV, Speed, and Sci-Fi Channel) have flourished despite the lack of exclusivity.<sup>325</sup>

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628(c)(2)(D). See *2002 Extension Order*, 17 FCC Rcd at 12153-54, ¶ 65 n. 206. We stated that (i) Section 628(c)(2)(D) places the burden on the party seeking exclusivity to show that an exclusive contract meets the statutory public interest standard and that no other program access provision provides this protection; (ii) these other provisions were all enacted as part of the 1992 Cable Act, indicating that, despite the existence of these other program access provisions, Congress found the exclusive contract prohibition to be necessary to preserve and protect competition and diversity; (iii) as compared to Section 628(c)(2)(D), Section 628(b) carries with it an added burden “to demonstrate that the purpose or effect of the conduct complained of was to ‘hinder significantly or to prevent’ an MVPD from providing programming to subscribers or customers”; (iv) conduct of undue influence necessary to establish a violation of Section 628(c)(2)(A) “may be difficult for the Commission or complainants to establish”; and (v) the prohibition of “non-price discrimination” in Section 628(c)(2)(B) requires the complainant to demonstrate the conduct was “unreasonable” which may be difficult to establish. See *id.* (citing *First Report and Order*, 8 FCC Rcd at 3424, ¶ 145). No commenter provides any basis for us to revisit these conclusions. Moreover, we note that some competitive MVPDs argue that allowing the exclusive contract prohibition to sunset would provide cable-affiliated programmers with an incentive to enter into exclusive contracts with their affiliated cable operators to avoid allegations of unfair acts or practices or discrimination with respect to their dealings with unaffiliated distributors. See *EchoStar Comments* at 11 n.22; *USTelecom Comments* at 13.

<sup>321</sup> See *Cablevision Comments* at 29 and Appendix B at 2 (arguing that exclusivity leads to beneficial “product differentiation,” whereby creators and distributors respond to exclusivity strategies of their rivals by producing and distributing distinct content offerings that enable them to maintain a unique presence in the marketplace); *Comcast Comments* at 13-18. Comcast notes that its competitor, DIRECTV, has used exclusive arrangements with various sports leagues as a competitive tool to attract customers away from cable operators. See *Comcast Comments* at 18.

<sup>322</sup> 47 U.S.C. § 548(c)(4); see also 47 C.F.R. § 76.1002(c)(4).

<sup>323</sup> See *New England Cable News Channel, Memorandum Opinion and Order*, 9 FCC Rcd 3231 (1994); *NewsChannel, Memorandum Opinion and Order*, 10 FCC Rcd 691 (CSB, 1994).

<sup>324</sup> See *Time Warner Cable, Memorandum Opinion and Order*, 9 FCC Rcd 3221, 3230, ¶ 55 (1994) (denying exclusivity petition for Courtroom Television (“Court TV”)); *Outdoor Life Network and Speedvision Network, Memorandum Opinion and Order*, 13 FCC Rcd 12226, 12242, ¶ 28 (CSB, 1998) (denying exclusivity petition for the Outdoor Life Network (“OLN”) and Speedvision Network (“Speedvision”)); *Cablevision Industries Corp. and Sci-Fi Channel, Memorandum Opinion and Order*, 10 FCC Rcd 9786, 9791, ¶ 32 (CSB, 1995) (denying exclusivity petition for the Sci-Fi Channel).

<sup>325</sup> The following data demonstrates that the three programming networks for which exclusivity was denied (Court TV, Speed, and Sci-Fi Channel) have prospered despite the lack of exclusivity. Court TV’s subscribership increased from 16.1 million in 1994 to 87.9 million in 2006, and its prime-time ratings increased from 0.15 in 1994 to 0.81 in 2005. See Kagan Research, LLC, *Economics of Basic Cable Networks – 13<sup>th</sup> Annual Edition* at 37-38, 50-52 (2007) (“*Kagan Report 13<sup>th</sup> Edition*”); Kagan Research, LLC, *Economics of Basic Cable Networks – 9<sup>th</sup> Annual Edition* at 42, 44 (2003) (“*Kagan Report 9<sup>th</sup> Edition*”). OLN’s (now known as Versus) subscribership increased from 18 (continued....)

### c. Impact on Programming

64. We find above that the exclusive contract prohibition continues to be necessary to preserve and protect diversity in the distribution of programming.<sup>326</sup> While cable MSOs contend that the exclusive contract prohibition reduces incentives for cable operators and competitive MVPDs to create and invest in new programming, we find no evidence to support this theory.<sup>327</sup> To the contrary, the number of vertically integrated satellite-delivered national programming networks has more than doubled since 1994 when the rule implementing the exclusive contract prohibition took effect<sup>328</sup> and has continued to increase since 2002 when the Commission last examined the exclusive contract prohibition.<sup>329</sup> Moreover, the number of national programming networks has increased by almost 400 percent since

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million in 1998 to 67.8 million in 2006. See *Kagan Report 13<sup>th</sup> Edition* at 37-38, 50-52. Speedvision's (now known as Speed) subscribership increased from 20 million in 1998 to 65.9 million in 2006. See *id.* The Sci-Fi Channel's subscribership increased from 27.4 million in 1995 to 88.1 million in 2006, and its prime-time ratings increased from 0.65 in 1995 to 1.04 in 2005, making it the fifteenth-ranked programming network by prime-time ratings. See *Kagan Report 13<sup>th</sup> Edition* at 37-38, 50-52; *Kagan Report 9<sup>th</sup> Edition* at 42, 44; see also *12<sup>th</sup> Annual Report*, 12 FCC Rcd at 2655, Table C-6; Qwest Reply Comments at 6-7 ("[N]otwithstanding the Commission's refusal to give them an exemption from Section 628(c)(2)(D)'s prohibition on exclusivity, [Speed and Versus] have grown to become two of the more popular 'niche-oriented' cable channels in circulation.").

<sup>326</sup> As we stated in the 2002 *Extension Order*, while we recognize that the exclusive contract prohibition's impact on programming diversity is one component of our analysis, Congress directed that "our primary focus should be on preserving and protecting diversity in the distribution of video programming -- i.e., ensuring that as many MVPDs as possible remain viable distributors of video programming." See 2002 *Extension Order*, 17 FCC Rcd at 12152, ¶ 62 (emphasis in original).

<sup>327</sup> Cablevision argues that the exclusive contract prohibition (i) deprives cable operators of the incentive to invest in new programming because the prohibition requires them to share the programming with their competitors; and (ii) deprives competitive MVPDs of the incentive to invest in programming because the prohibition provides them with access to programming developed by their competitors. See Cablevision Comments at 10, 27-29 and Appendix B at 26-27. Cablevision and Comcast also argue that some new MVPDs, such as AT&T and Verizon, have sufficient resources to invest their own programming. See Cablevision Comments at 5, 10, 29; Comcast Reply Comments at 6.

<sup>328</sup> Compare *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, First Report and Order, 9 FCC Rcd 7442, 7589-92 (1994) ("1<sup>st</sup> Annual Report") (56 vertically integrated national programming networks) with *12<sup>th</sup> Annual Report*, 21 FCC Rcd at 2575, ¶ 157 (116 vertically integrated national programming networks).

<sup>329</sup> Compare 2002 *Extension Order*, 17 FCC Rcd at 12131-32, ¶ 18 (citing *8<sup>th</sup> Annual Report*, 17 FCC Rcd at 1309-10, ¶ 157 (104 vertically integrated national programming networks)) with *12<sup>th</sup> Annual Report*, 21 FCC Rcd at 2575, ¶ 157 (116 vertically integrated national programming networks); see EchoStar Comments at 4 ("The number of new vertically integrated programming networks since 2002 described herein undercuts any suggestion that this prohibition prevents or limits the ability or desire of cable conglomerates to create new programming assets."); USTelecom Comments at 19; Verizon Reply Comments at 4 ("[N]o reasonable basis exists for the Commission to conclude that the exclusive contract prohibition has had or will have any adverse impact on the development of programming, particularly when experience proves otherwise."); see also Letter from Stephanie L. Podey, Counsel for Comcast Corporation, to Ms. Marlene H. Dortch, FCC, MB Docket Nos. 07-29, 06-189 (June 13, 2007), Attachment at 3 (stating that "Comcast continues to invest in new programming networks" and noting Comcast's partnering in 2006 with CSTV to launch The mtn., a national network dedicated to sports programming, as well as Comcast's investment in additional regional sports networks); EchoStar Comments at 7-8 (noting new vertically integrated cable networks launched since 2002).

1994<sup>330</sup> and by 80 percent since 2002.<sup>331</sup> There is also evidence that some competitive MVPDs have begun to invest in their own programming despite their ability to access cable-affiliated programming based on the exclusive contract prohibition and the program access rules.<sup>332</sup> Accordingly, we find no basis to conclude that extending the exclusive contract prohibition will create a disincentive for the creation of new programming.<sup>333</sup>

65. We are mindful that our decision to extend the exclusive contract prohibition must withstand an intermediate scrutiny test pursuant to First Amendment jurisprudence.<sup>334</sup> As the D.C. Circuit explained in rejecting a facial challenge to the constitutionality of the exclusive contract prohibition in Section 628(c)(2)(D), the prohibition will survive intermediate scrutiny if it “furthers an important or substantial governmental interest; if the governmental interest is unrelated to the suppression of free expression; and if the incidental restriction on alleged First Amendment freedoms is no greater than is essential to the furtherance of that interest.”<sup>335</sup> For the reasons discussed herein, our decision to extend the exclusive contract prohibition satisfies this intermediate scrutiny test. First, in *Time Warner*, the court found that the governmental interest Congress intended to achieve in enacting the exclusive contract prohibition was “the promotion of fair competition in the video marketplace,” and that this interest was substantial.<sup>336</sup> Moreover, the court noted Congress’ conclusion that “the benefits of these provisions -- the increased speech that would result from fairer competition in the video programming marketplace -- outweighed the disadvantages [resulting in] the possibility of reduced economic incentives to develop new programming.”<sup>337</sup> We disagree with cable MSOs to the extent they argue that the substantial government interest in achieving competition in the video distribution market has been met.<sup>338</sup> As discussed above, cable operators still have a dominant share of MVPD subscribers (approximately 67

<sup>330</sup> Compare 1<sup>st</sup> Annual Report, 9 FCC Rcd at 7589-92 (107 satellite-delivered national programming networks) with 12<sup>th</sup> Annual Report, 21 FCC Rcd at 2575, ¶ 157 (531 satellite-delivered national programming networks).

<sup>331</sup> Compare 2002 Extension Order, 17 FCC Rcd at 12131-32, ¶ 18 (citing 8<sup>th</sup> Annual Report, 17 FCC Rcd at 1309-10, ¶ 157 (237 satellite-delivered national programming networks)) with 12<sup>th</sup> Annual Report, 21 FCC Rcd at 2575, ¶ 157 (531 satellite-delivered national programming networks).

<sup>332</sup> For example, Verizon has invested in new programming for its FiOS TV service. In March 2007, Verizon announced that it was launching FiOS1, a local television channel for FiOS TV subscribers in the Washington, DC metropolitan area that offers local weather, traffic, news, sports, and community features. See FiOS1, Verizon’s First Local TV Channel. Debuts in Washington, D.C., Metro Area. FiOS TV Subscribers to Get Local Information, Sports and Features All Day on FiOS1. <http://newscenter.verizon.com/press-releases/verizon/2007/fios1-verizons-first-local.html> (last visited July 27, 2007). Verizon also announced that it expects to launch similar channels in other markets this year. See *id.*

<sup>333</sup> See 2002 Extension Order, 17 FCC Rcd at 12153, ¶ 64.

<sup>334</sup> See Cablevision Comments at 10; Comcast Reply Comments at 3; NCTA Reply Comments at 8-10; Time Warner Reply Comments at 20-21.

<sup>335</sup> *Time Warner Entertainment Co. L.P. v. FCC*, 93 F.3d 957, 978 (D.C. Cir. 1996) (quoting *Turner Broadcasting System, Inc. v. FCC*, 512 U.S. 622, 662 (1994) (quoting *United States v. O’Brien*, 391 U.S. 367, 377 (1968))).

<sup>336</sup> *Id.* Moreover, one of Congress’ express findings in enacting the 1992 Cable Act was that “[t]here is a substantial governmental and First Amendment interest in promoting a diversity of views provided through multiple technology media.” Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (1992), § 2(a)(6).

<sup>337</sup> *Time Warner Entertainment Co. L.P.*, 93 F.3d at 979 (citing S. Rep. No. 92, 102d Cong., 2d Sess. 4 (1991), at 26-28, reprinted in 1992 U.S.C.C.A.N. 1133, 1159-61).

<sup>338</sup> See NCTA Reply Comments at 9-10.

percent), have raised prices in excess of inflation despite the emergence of new competitors,<sup>339</sup> and still own significant programming networks.<sup>340</sup> Accordingly, we conclude that competition and diversity in the video distribution market has not reached the level at which Congress intended the exclusive contract prohibition would sunset.<sup>341</sup> Second, in *Time Warner*, the court held that the governmental objective in adopting the exclusive contract prohibition in Section 628(c)(2)(D) was unrelated to the suppression of free speech.<sup>342</sup> In this *Order*, we extend the exclusive contract prohibition for an additional five years but do not otherwise modify the prohibition. Thus, the prohibition remains unrelated to the suppression of free speech, as the D.C. Circuit Court of Appeals previously held.<sup>343</sup> Third, in *Time Warner*, the court rejected claims that the exclusive contract prohibition was not narrowly tailored to achieve the stated government interest.<sup>344</sup> In this *Order*, we extend the exclusive contract prohibition for a term of five years but do not otherwise modify the prohibition. Thus, the prohibition remains narrowly tailored to meet the statute's objective, and any incidental restriction on alleged First Amendment freedoms is no greater than is essential to the furtherance of that objective.<sup>345</sup>

66. We note that cable MSOs argue that the exclusive contract prohibition is not narrowly tailored because it is allegedly both overinclusive (in that it applies to "new," "unpopular," and other types of programming that are arguably not essential to the viability of competition in the video distribution market) and underinclusive (in that it does not apply to certain non-cable-affiliated programming that may be necessary for viable competition in the MVPD market).<sup>346</sup> We reject proposals to modify the scope of the exclusive contract prohibition for the reasons discussed in Section III.A.4. Moreover, we note that the exclusive contract prohibition in Section 628(c)(2)(D) is not absolute. Rather, cable-affiliated programmers may seek approval to enter into exclusive programming contracts that satisfy the criteria set forth by Congress in Section 628(c)(2) and (4).<sup>347</sup> Thus, requests to enter into exclusive contracts for "new," "unpopular," and other types of programming cited by cable MSOs as non-essential to the viability of competition can be addressed through individual exclusivity petitions.<sup>348</sup> Finally, as discussed above, we have found no evidence that the exclusive contract prohibition is creating

<sup>339</sup> See 2006 Cable Price Report, 21 FCC Rcd at 15087-88, ¶ 2 ("Overall, cable prices increased more than 5 percent last year and by 93 percent since the period immediately prior to Congress's enactment of the Telecommunications Act of 1996. Expanded basic prices rose more than 6 percent or twice the rate of inflation last year.").

<sup>340</sup> See *supra* Section III.A.2.

<sup>341</sup> See AT&T Reply Comments at 13 n.48 (stating that the exclusive contract prohibition continues to materially advance an important or substantial government interest).

<sup>342</sup> See *Time Warner Entertainment Co. L.P.*, 93 F.3d at 978 ("[T]he vertically integrated programming provisions apply to only a limited number of companies for a perfectly legitimate reason: the antitrust concerns underlying the statute arise precisely because the number of vertically integrated companies is small. The vertically integrated programmer provisions are thus not 'structured in a manner that raise[s] suspicions that their objective was, in fact, the suppression of certain ideas.'" (quoting *Turner*, 512 U.S. at 660, 114 S.Ct. at 2468)).

<sup>343</sup> See *id.* at 978.

<sup>344</sup> See *id.* at 978-79.

<sup>345</sup> See *id.*

<sup>346</sup> See Comcast Reply Comments at 3; NCTA Reply Comments at 9.

<sup>347</sup> 47 U.S.C. § 548(c)(2) and (4).

<sup>348</sup> As noted above, only ten exclusivity petitions have been filed to date. See *supra* ¶ 63. Of these petitions, two were granted, three were denied, and five were dismissed at the request of the parties.

a disincentive for the creation of new programming.<sup>349</sup> Despite claims that the exclusive contract prohibition deprives cable operators and others of the incentive to invest in new programming, thereby restricting the creation of new programming, the record reflects the opposite.<sup>350</sup> Thus, contrary to these contentions, the prohibition has fostered, not restricted, speech.

#### 4. Scope of Exclusive Contract Prohibition

67. Various commenters argue that the exclusive contract prohibition is both overinclusive and underinclusive with respect to the type of programming and MVPDs it covers. Some commenters ask the Commission to either narrow or expand the scope of the prohibition accordingly. Some cable MSOs argue that this alleged overinclusiveness and underinclusiveness render the exclusive contract prohibition arbitrary and capricious under the Administrative Procedures Act.<sup>351</sup> As discussed below, we decline to either narrow or expand the exclusive contract prohibition.

##### a. Narrowing the Prohibition

###### (i) Narrowing Based on Status of Programming Network

68. For the reasons discussed below, we decline to narrow the scope of the exclusive contract prohibition based on the status of the programming network. The exclusive contract prohibition in Section 628(c)(2)(D) and the implementing rules pertain to all satellite-delivered programming networks that are vertically integrated with a cable operator, regardless of their popularity. Some cable MSOs argue that the prohibition is thus overinclusive because it includes new and unpopular programming networks that are not essential to the ability of an MVPD to compete. These cable MSOs ask the Commission to narrow the scope of the exclusion contract prohibition based on the status of the programming network by (i) allowing exclusive arrangements for new and unpopular programming;<sup>352</sup> (ii) allowing exclusive arrangements for regional non-sports programming;<sup>353</sup> and (iii) allowing exclusive arrangements for RSNs in DMAs served by more than one unaffiliated RSN.<sup>354</sup>

69. As an initial matter, we note that in adopting the exclusive contract prohibition in Section 628(c)(2)(D), Congress applied the prohibition to all cable-affiliated programming. Congress did not distinguish between different types of cable-affiliated programming. Instead, Congress in Section 628(c)(4) established criteria whereby cable-affiliated programmers could petition the Commission for authority to enter into exclusive arrangements despite the general rule prohibiting all such exclusive

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<sup>349</sup> See *supra* ¶ 63.

<sup>350</sup> See *id.*

<sup>351</sup> See, e.g., Cablevision Comments at 30-32; Comcast Comments at 24-26; Comcast Reply Comments at 25-28. These cable MSOs also raise First Amendment concerns, which we address above in Section III.A.3.c.

<sup>352</sup> See Cablevision Comments at 31 (arguing that the following types of programming cannot be considered necessary to protect competition: (i) national networks with low average prime-time ratings; (ii) new programming services since they cannot be considered essential to the “continued” viability of competing MVPDs; and (iii) cable networks that are not deemed important by market participants to warrant carriage to a significant number of households).

<sup>353</sup> See *id.* (stating that the Commission concluded in the *Adelphia* proceeding that access to regional non-sports programming is not essential to competition, citing *Adelphia Order* (21 FCC Rcd at 8279, ¶ 169)).

<sup>354</sup> See *id.* (arguing that where RSNs are competing for sporting events, there is little risk that an exclusive arrangement for one network will foreclose competition).

arrangements.<sup>355</sup> Requests to remove certain cable-affiliated programming networks from the prohibition can be addressed through these individual exclusivity petitions.<sup>356</sup> Accordingly, as the Commission concluded in the 2002 *Extension Order*, we believe that treating all satellite cable programming and satellite broadcast programming uniformly for purposes of the exclusive contract prohibition is consistent with Section 628(c)(2)(D) and the definitions set forth in Sections 628(i)(1) and (3).<sup>357</sup> Moreover, no commenter has provided a rational and workable definition of “must have” programming that would allow us to apply the exclusive contract prohibition to only this type of programming. In the 2002 *Extension Order*, the Commission recognized “the difficulty of developing an objective process of general applicability to determine what programming may or may not be essential to preserve and protect competition” and further noted that any attempt to distinguish between different types of cable-affiliated programming is likely to raise Constitutional concerns.<sup>358</sup> Cable MSOs asking us to narrow the scope of the prohibition suggest no workable mechanisms for alleviating these concerns.

#### (ii) Narrowing Based on Status of Cable Operator

70. For the reasons discussed below, we decline to narrow the scope of the exclusive contract prohibition based on the status of the cable operator. Cable MSOs argue that we should narrow the exclusive contract prohibition by allowing certain types of exclusive arrangements based on the status of the cable operator, such as (i) those involving an affiliated cable operator whose network passes only a small number of households throughout the nation;<sup>359</sup> (ii) those between a cable operator and an affiliated programming network outside the footprint of the affiliated cable operator;<sup>360</sup> and (iii) those involving affiliated cable operators that face competition from both DBS and telephone companies.<sup>361</sup>

71. In adopting the exclusive contract prohibition in Section 628(c)(2)(D), Congress applied the prohibition to *all* cable operators. Congress did not distinguish between different types of cable operators for purposes of Section 628(c)(2)(D). Moreover, in adopting the exclusive contract prohibition, Congress has already delineated a geographic demarcation applicable to the prohibition – “areas served

<sup>355</sup> See 47 U.S.C. § 548(c)(4); 47 C.F.R. § 76.1002(c)(4).

<sup>356</sup> We remind those cable MSOs urging exemption of certain types of programming from the exclusive contract prohibition that the Commission will entertain individual exclusivity petitions as Congress mandated. See 47 U.S.C. § 548(c)(4); 47 C.F.R. § 76.1002(c)(4). In the 2002 *Extension Order*, we provided an example of one type of vertically integrated programming that may qualify for exclusivity. See 2002 *Extension Order*, 17 FCC Rcd at 12135-36, ¶ 25 (“if a vertically integrated programmer contemplates the introduction of innovative services with limited or niche audiences and believes that these services will not be economically viable without a period during which they are offered on an exclusive basis, we encourage such programmer to petition the Commission to approve a period of exclusivity”).

<sup>357</sup> See 2002 *Extension Order*, 17 FCC Rcd at 12156, ¶ 69.

<sup>358</sup> *Id.*

<sup>359</sup> See Cablevision Comments at 30-31.

<sup>360</sup> See Cablevision Comments at 30-31; Time Warner Reply Comments at 20.

<sup>361</sup> See Cablevision Comments at 31-32.



by a cable operator.”<sup>362</sup> Congress did not provide that the exclusive contract prohibition should vary based on the competitive circumstances in individual geographic areas served by a cable operator.<sup>363</sup>

72. We also find that these attempts to narrow the exclusive contract prohibition would harm competition in the video distribution marketplace. One of the key anticompetitive practices that the exclusive contract prohibition addresses is the practice of leveraging cable’s market power collectively by withholding affiliated programming from rival MVPDs while selling the affiliated programming to other cable operators which do not compete with one another. A cable operator may gain by weakening a current or potential rival (such as a DBS operator) even in markets that the cable operator itself does not serve.<sup>364</sup> Thus, proposals to narrow the exclusive contract prohibition by allowing exclusive arrangements outside of the footprint of the affiliated cable operator or with cable operators whose networks pass only a small number of households throughout the nation will impede competition in the video distribution marketplace. We similarly find that allowing exclusive arrangements for affiliated cable operators that face competition from both DBS and telephone companies would harm competition in the video distribution marketplace. We conclude herein that a cable operator will not lose the incentive and ability to enter into an exclusive arrangement in a given geographic area simply because it faces competition from both DBS operators and telephone companies in that area. As discussed above, the key consideration is the market share of the cable operator relative to other competitors. Indeed, in areas where a telephone company has recently entered the video distribution market, its market share will be minimal, providing cable operators with the ability and incentive to enter into exclusive arrangements that adversely impact competition.<sup>365</sup>

### (iii) Narrowing Based on Status of Competitive MVPD

73. For the reasons discussed below, we decline to narrow the exclusive contract prohibition by precluding certain competitive MVPDs from benefiting from the prohibition. Comcast and Cablevision ask us to narrow the exclusive contract prohibition by precluding certain competitive MVPDs from benefiting from the prohibition, such as competitive MVPDs that (i) have been in the MVPD market

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<sup>362</sup> 47 U.S.C. § 548(c)(2)(D); *see also* 2002 Extension Order, 17 FCC Rcd at 12156-57, ¶ 70.

<sup>363</sup> We again note that through individual exclusivity petitions, the Commission may determine (in accordance with statutory criteria) whether a particular exclusive contract, otherwise prohibited under Section 628(c)(2)(D), is in the public interest. *See* 47 U.S.C. § 548(c)(4); 47 C.F.R. § 76.1002(c)(4).

<sup>364</sup> *See* 2002 Extension Order, 17 FCC Rcd at 12140-41, ¶¶ 36-39; *see also* DIRECTV Comments at 8-9; CA2C Reply Comments at 7.

<sup>365</sup> *See supra* ¶ 60 (discussing incentives of vertically integrated cable programmers to withhold programming from recent entrants in the video marketplace).

for more than five years;<sup>366</sup> (ii) have extensive resources;<sup>367</sup> or (iii) enter into exclusive contracts for programming.<sup>368</sup>

74. Section 628 makes no distinction among MVPDs of the kind suggested by these commenters. Moreover, we find that adopting such restrictions on the entities that can benefit from the prohibition will limit competition in the video distribution market<sup>369</sup> and will result in no discernible public interest benefits.<sup>370</sup> The resources of competitors or the number of years they have spent in the market has no bearing on the goal of Section 628(c)(2)(D) to preclude exclusive contracts in order to facilitate competition in the video distribution market. Rather, if cable operators have exclusive access to non-substitutable content that is essential for viable competition and they have the incentive to withhold such content, the amount of resources of competitive MVPDs or their longevity in the market will not be able to overcome that competitive advantage.<sup>371</sup> Comcast asks us to prevent competitive MVPDs that themselves enter into exclusive programming contracts from being the beneficiaries of the exclusive contract prohibition applied to cable-affiliated programmers.<sup>372</sup> Section 628, however, does not exempt cable operators from its restrictions based on the contracting practices of non-cable MVPDs.

#### **b. Expanding the Prohibition**

##### **(i) Expanding the Prohibition to Non-Cable-Affiliated Programming**

75. For the reasons discussed below, we decline to apply an exclusive contract prohibition to non-cable-affiliated programming. The exclusive contract prohibition in Section 628(c)(2)(D) and the implementing rules pertain only to programming networks that are vertically integrated with a "cable

<sup>366</sup> See Comcast Comments at 26 (stating that, after five years in the video distribution business, "a competitor should be able to sink or swim on its own"); see also Cablevision Comments at 5 ("Cablevision faces competition from two DBS providers, each of which has a subscriber base at least four times larger than its own . . . . Each of those entities has the ability to invest in its own programming, just as Cablevision did.").

<sup>367</sup> See Comcast Comments at 26 (arguing that the benefits of the exclusive contract prohibition should not be available to a company with over 10 million customers or to a company that is part of an enterprise with a market capitalization of over \$100 billion); see also Cablevision Comments at 5 ("Cablevision faces competition from . . . Verizon and AT&T, whose market capitalizations are 10 and 25 times larger, respectively, than Cablevision's. Each of those entities has the ability to invest in its own programming, just as Cablevision did.").

<sup>368</sup> See Comcast Comments at 26.

<sup>369</sup> See AT&T Reply Comments at 12-13 (stating that proposals by Cablevision and Comcast to narrow the exclusive contract prohibition "would gut the rule precisely where it might be of use to competitors with a viable opportunity to offer consumers a real alternative to cable: those with experience, those with capital, and those with a foothold in the market"); CA2C Reply Comments at 9 (stating that these proposals would "ensure that the rules have no application to any significant competitor" that Cablevision and Comcast face, thereby "making sure the rules are meaningless"); Verizon Reply Comments at 12-13.

<sup>370</sup> See *supra* Section III.A.3.c (concluding that there is no evidence that the exclusive contract prohibition has had an adverse impact on the incentives for creation of new programming).

<sup>371</sup> See Verizon Reply Comments at 11-12 ("That a new video entrant may have a large market capitalization or a sizeable number of telephone customers does not ensure competitive success in the video market when the entrant cannot offer the programming subscribers want to see.").

<sup>372</sup> See Comcast Comments at 26.